European Commission - Press release

State aid: Commission approves impaired asset management measures for banks in Hungary and Italy

Brussels, 10 February 2016

The Commission concluded that the pricing models used by the Hungarian asset management company ensure it will buy non-performing loans at market prices. The Commission also decided that under the state guarantee scheme chosen by the Italian authorities, the State will be remunerated in line with market conditions for the risk it will assume by granting a guarantee on securitised non-performing loans. This formalises an understanding reached between Commissioner Vestager and Minister Padoan on 26 January 2016.

If a Member State intervenes as a private investor would do and is remunerated for the risk assumed in a way a private investor would have accepted, then such interventions do not constitute state aid. The Commission therefore concluded that neither the Hungarian nor the Italian measures involve state aid within the meaning of the EU rules.

Commissioner **Margrethe Vestager**, in charge of competition policy, stated: "*Today's decisions show that EU rules offer Member States different tools to kick-start the clean-up of bank balance sheets, either with or without the use of state aid. The Commission's role is simply to ensure that the choice made by the national government does not unduly burden the public purse or distort the level playing field in the EU.*"

Vice-President **Valdis Dombrovskis,** responsible for the Euro and Social Dialogue, said: "*High levels of non-performing loans in some Member States are weighing on banks' balance sheets and hampering their ability to lend to businesses and households. This has also been highlighted in the past, not least in recommendations of the European Commission. The measures planned by the Hungarian and Italian authorities and approved by the Commission show that Member States are paying more attention to this issue, and demonstrate the possibility to design solutions that do not rely on state aid. The effectiveness of these schemes will be improved by flanking reforms in the banking sector and the wider economy*."

Hungarian Bad Bank

MARK is a Hungarian asset management company to which solvent financial institutions in Hungary can, on a voluntary basis, decide to sell at market price a specific pool of non-performing loans backed by commercial real estate. MARK will apply a specific valuation method to determine the market price of these assets. It is intended to kick-start the workout of certain non-performing loans held by banks in Hungary. The budget of MARK has initially been set at €1 billion, which may be increased at a later stage.

In particular, MARK will buy non-performing loans collateralised by commercial real estate assets, such as offices, hotels, retail projects (such as shopping centres), land plots and industrials (such as warehouses). The Commission's assessment has shown that MARK's methodology to determine the transfer price will ensure a market conform valuation:

- First, the Commission concluded that the **granular valuation models** developed by MARK **for each asset category** establish prices at market conditions. They are based on prudent parameters and generally accepted valuation methods. Moreover, the models were calibrated on the basis of the most recent market transaction prices available.
- Second, MARK will hire an **independent valuer** to perform the valuations based on the valuation models, which will be double-checked by a qualified validator.
- Third, additional safeguards, including **a cap on the transfer price** and **ex-post verification of transactions**, will further ensure that the actual transactions do not involve state aid.

The Commission has therefore concluded that the measure is free of state aid within the meaning of EU state aid rules. This decision takes no position on compliance with other legal aspects in relation to MARK's set-up, funding and governance.

Italian state guarantee scheme

The Italian state guarantee scheme is designed to assist Italian banks in securitising and moving non-performing loans off their balance sheets. An individually managed, private securitisation vehicle would buy non-performing loans from the bank, pool them, and sell notes to the securitised assets it holds at different risk levels to investors, i.e. risk-bearing junior and – optional – mezzanine notes, as well as lower-risk senior notes, which in addition would benefit from a State guarantee. The objective is to attract a wide range of investors, incentivise banks to workout non-performing loans as quickly as possible, and improve their liquidity.

The Commission's assessment showed that the State guarantees on the senior notes will be remunerated at market terms according to the risk taken, i.e. in a manner acceptable for a private operator under market conditions. This is in particular ensured by the following elements:

- First, the **risk for the State will be limited** since the state guarantee only applies to the senior tranche. An ECB-approved independent rating agency would ensure that notes of the senior tranche, without taking into account the State guarantee, correspond to an investment-grade risk. The ability of the securitisation vehicle to repay the senior tranche will depend on, amongst other things, the work-out rates of the underlying assets, costs of the securitisation vehicle, thickness of junior and – if present – mezzanine tranches and quality of the servicer.
- Second, the risk distribution of the tranches and the set-up of the securitisation entities will be **tested and confirmed by the market before the State assumed any risk**. The State guarantee on the senior tranche will only become effective, if at least more than half of the non-guaranteed and risk-bearing junior tranche has been successfully sold to private market participants.
- Third, the State's **remuneration for the risk taken will be at market terms**. The guarantee fee will be based on a market benchmark (a basket of credit default swap prices of Italian based companies) and correspond to the level and duration of the risk the State takes granting the guarantee. This means that the guarantee fee paid will increase over time in line with the duration of the State's exposure. This fee structure in addition to the appointment of an external servicer aims to increase the efficiency of the workout and likely recovery on the non-performing loans.

On this basis, the Commission was able to conclude that the measure is free of state aid within the meaning of EU state aid rules.

Background

Under EU law there are possibilities for Member States to implement impaired asset measures to deal with non-performing loans both with and without the use of state aid. The choice of the type of intervention lies with the Member State and it is always the decision of the Member State whether to grant any state aid. The Commission, as the body responsible for EU state aid control, has to ensure that any measure implemented is in line with EU rules.

If a Member State chooses to intervene in a bank as a private investor would do, then such an intervention would not constitute state aid and falls outside of EU State aid control. In that case, the Commission verifies that the State does not bear any more risk than a private investor would have taken and paid for.

If, conversely, the State pays above market prices for the non-performing loans or accepts lower guarantees fees than a private operator would have done, then this constitutes state aid and can only be implemented if the bank is put into resolution, in compliance with EU State aid rules and relevant requirements under bank recovery and resolution rules.

The non-confidential version of the decisions will be published in the State aid register on the competition website under the case number SA.38843 (Hungary) and SA.43390 (Italy) once confidentiality issues have been resolved. The State Aid Weekly e-News lists new publications of state aid decisions on the internet and in the EU Official Journal.

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